85-1540

Supreme Court, U.S.
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NO. _____

IN THE SUPREME COURT OF THE
UNITED STATES

October Term, 1985

MID-STATE HOMES, INC.,
PETITIONERS

VS.

UNITED STATES OF AMERICA,
RESPONDENT

PETITION FOR A WRIT OF
CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR
THE ELEVENTH CIRCUIT
(FROM A FINAL JUDGMENT
ENTERED ON DECEMBER 5, 1985)

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Petitioner, Mid-State Homes, Inc. respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Eleventh Circuit entered in this proceeding on September 13, 1985.

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OPINIONS AND ORDERS BELOW

The opinion of the District Court was filed on May 23, 1984, a copy of which is appended to this petition as Exhibit "A". This opinion was based on the District Court's earlier ruling in Southern Bank of Lauderdale County v. Internal Revenue Service, United States of America, CV 82-HM-5236-NW, 84-1 U.S.T.C. para. 9245 (N.D.Ala.1984) filed on February 14, 1984. A copy of the Southern Bank order is appended hereto as Exhibit "B". The initial opinion of the Eleventh Circuit Court of Appeals in both cases was issued September 13, 1985. A copy of that opinion is appended hereto as Exhibit "C". A subsequent opinion of the Eleventh Circuit Court of Appeals denying Petitioner's Request for Rehearing and Suggestion for En Banc Consideration was issued on December 5, 1985. A

copy of that opinion is appended hereto as Exhibit "D".

JURISDICTION

This Court has jurisdiction to grant the petition pursuant to Rule 19 of the Rules of the Supreme Court of the United States. Petitioner further invokes the jurisdiction of this Court on the basis that an important question is presented with regard to the application and interpretation of 26 U.S.C. Section 7425 and whether the interpretation made by the Eleventh Circuit results in a taking of Petitioner's property in violation of Petitioner's constitutional rights under the 5th Amendment of the Constitution of the United States.

The jurisdiction of this Court is invoked under 28 U.S.C. Section 1291.

QUESTIONS PRESENTED

1. Whether a valid first mortgage holder's rights can be lost or taken by the Government following a foreclosure sale, made without notice to the Government pursuant to 26 U.S.C. Section 7425.

2. Whether a foreclosure sale made without notice to the Government pursuant to 26 U.S.C. Section 7425, results in the Government acquiring more rights in the property then the taxpayer held, contrary to prior holdings of this Court.

STATUTORY PROVISIONS INVOLVED

26 U.S.C. Section 7425. That statute is attached as Exhibit "E" of this petition.

STATEMENT OF THE CASE

Petitioner was a senior mortgagee on a parcel of land in Alabama. Following the recording of Petitioner's mortgage, the Government filed a tax lien against the mortgaged property. Upon default of the mortgage, Petitioner foreclosed without giving notice to the Government. The Government thereafter levied on the property claiming its interest to be superior to the interest of Petitioner. Petitioner filed its complaint in District Court seeking to declare Section 7425 unconstitutional, to enjoin enforcement of the Government's lien and to have the property returned to Petitioner.

Petitioner's motion for summary judgment was granted in this case on May 23, 1984. The Government filed its Notice of Appeal on July 17, 1985. On

September 13, 1985, a panel of the Eleventh Circuit rendered its opinion, reversing the judgment of the District Court. A petiton for rehearing and for en banc consideration followed. The Eleventh Circuit Court of Appeals issued its opinion denying the petition on December 5, 1985.

STATEMENT OF THE FACTS[1]

The facts in this case are undisputed. Petitioner obtained a valid first lien, and, under Alabama law, the legal title to a parcel of land, by virtue of the execution and assignment of a mortgage upon which the taxpayers were obligated. This mortgage was properly recorded under Alabama law. (R. 39, 42,

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[1]"RR." references are to the pages of the single volume of the original record on appeal of case 84-7501, as paginated by the Clerk of the District Court and transmitted to this Court.

111-112). Thereafter, the Internal Revenue Service made assessments against the taxpayers for unpaid taxes and filed notices of the federal tax liens pursuant to 26 U.S.C. Section 6323. (R. 111-112).

The taxpayers defaulted on their mortgage. Thereafter, Petitioner conducted a nonjudicial foreclosure sale in accordance with the power of sale contained in the mortgage. Such a sale is in all respects valid and proper under state law. In connection with the foreclosure, Petitioner admits that it did not provide the United States with notice of the sale as required under 26 U.S.C. Section 7425. Nor did the United States consent to the sale. Petitioner was the purchaser of the property at the non-judicial sale, and, under state law, the foreclosure and sale to Petitioner,

cut off all rights of the taxpayers mortgages, except a statutory right of redemption, Code of Alabama (1975) Section 6-5-230.

Recognizing that its foreclosure sale was ineffectual and not valid against the Government, if 26 U.S.C. Section 7425 were valid and applicable, Petitioner conducted another foreclosure sale on November 30, 1982, approximately eleven months after the first foreclosure sale. (R. 112.) This time Petitioner gave notice of the sale to the Government pursuant to 26 U.S.C. Section 7425 (R. 112.) Petitioner again purchased at the foreclosure sale, and recorded its foreclosure deed on December 9, 1982. (R. 109, 112.)

The Government thereafter posted a notice of seizure upon the property and took possession.

REASONS FOR GRANTING THE WRIT

26 U.S.C. SECTION 7425 IS NOT INTENDED TO ALLOW THE GOVERNMENT, IN CONFLICT WITH PRIOR DECISIONS OF THIS COURT TO ACQUIRE MORE RIGHTS IN PROPERTY THAN THAT POSSESSED BY THE TAXPAYER AND TO CAUSE THE FORFEITURE OF THE SENIOR MORTGAGEE'S PRIOR RIGHTS

This issue merits Supreme Court consideration because its resolution involves two important questions. The first question involves interpretation of 26 U.S.C. Section 7425. This interpretation can only be made after answering the question of what law, state or federal, determines and creates property rights. Petitioner contends that the interpretation of Section 7425 by the Eleventh Circuit conflicts with earlier decisions of this Court and results in confiscation of Petitioners property without compensation.

The Eleventh Circuit's holding goes far beyond this particular case. This ruling, if allowed to stand, will have nationwide application and will effect the stability of land titles across the country.

In the context of a non-judicial foreclosure sale, Section 7425(b)(1) and (c)(1) require that the Government be given notice of the sale not less than 25 days prior to such sale. The form of notice prescribed by the Secretary mandates that the foreclosing party attach a copy of the Government's lien, set forth the name and address of the taxpayer, describe the property, list the approximate amount of the principal obligation, with interest, secured by the lien sought to be enforced, and give other information. Treas. Reg. Section 301.7425-3(d). This requires that each

mortgagee, prior to foreclosure, conduct another search of the property records to determine if a tax lien has been filed after the date of the recording of its mortgage. Such lien could not effect the validity or prime of the mortgage but according to the Eleventh Circuit, if a foreclosure is conducted without notice to the Government, the junior tax lien is catapulted to a superior and first interest in the property. If the mortgagee fails to give this detailed notice, to the Government(of the Government's own lien), the foreclosure sale shall be "made subject to and without disturbing" the Government's lien. That is the critical language of Section 7425.

The Eleventh Circuit decision in effect, creates a new property right in the Government not recognized by state

law nor failry provided by Section 7425. As a result of the ruling of the Eleventh Circuit, if a mortgagee forecloses its mortgage when there exists a federal tax lien junior to that mortgage, but fails to give notice of foreclosure the Internal Revenue Service, the mortgagee forfeits its interest in the property and title thereto is vested in the Government, giving the government a much greater property interest than it had, and effectively destroying the first mortgage holder's rights.

Petitioner contends that such a holding results in an unconstitutional taking of Petitioner's property without compensation, thus denying Petitioner's due process rights. However, if the Eleventh Circuit had followed this Court's earlier decisions, Section 7425 would be, and should be, so interpreted

to provide the Government the protection reasonably intended by Congress without resulting in an unconstitutional taking or forfeiture of Petitioner's property.

The Eleventh Circuit's ruling goes beyond the intent and requirement of 26 U.S.C. Section 7425, and violates previous holdings of this Court. The legislative history of Section 7425 indicates that Congress only intended to give "the Government an opportunity to review its position and determine the appro-priate action without placing an undue burden on a foreclosing creditor". 1966-2 Cum.Bull. 815, 832-833.

Moreover, this Court has consistently held that, under our federal constitutional division of power, state law defines and creates property interests. The Government's lien and remedies attach to the "taxpayer's state

- created interests". Aquilino v. United States, 363 U.S. 509, 513, 80 S.Ct. 1277, 4 L.Ed.2d 1365 (1960). And we submit, they attach to nothing more. The Eleventh Circuit seemingly recognized this in its Opinion but its holding ignores and bypasses the state created interest to allow the lien of the Government to attach to another and greater interest.

The Eleventh Circuit recognized that the only interest held by the taxpayer under Alabama law was an equitable right of redemption, but then ignored that interest to hold that the Government's lien "attached to the property in question"(emphasis added) and, after the foreclosure, was "an enforceable lien against the realty" (emphasis added). The state law distinction between the "equity of redemption" (being that

interest held by the mortgagor/taxpayer) and the fee simple title to the realty itself (being that interest held by the mortgagee) is critical to a proper interpretation of Section 7425, and is a distinction that cannot be sloughed over.

In United States v. Durham Lumber Company, 363 U.S. 522, 527 (1960), this Court held that a tax lien attaches only to the property interest of the taxpayer as defined by state law, and that the Government is entitled to recover only the amount which would have been available to the taxpayer. Under Alabama law the "[e]xecution of a mortgage passes legal title to the mortgagee. (citations omitted). The mortgagor is left with an equity of redemption . . .". Trauner v. Lowery, 369 So.2d 531, 534 (1979). As such, the taxpayer's only rights with

respect to the property (to which the lien may attach) consist of the right of use and possession against the world (except as to the mortgagee, Petitioner); Jones v. Butler, 286 Ala. 69, 71, 237 So.2d 460, 462 (1970); and the right to redeem by paying the mortgage debt. Zimmerman v. Peoples Bank of Mobile, 23 Ala. 21, 81 So. 811 (1919). Since the only interest the taxpayers held prior to foreclosure was an equity of redemption, the Government's lien can attach only to that equity of redemption as opposed to the realty itself. The Eleventh Circuit's opinion, by holding that the Government's lien attached to an interest other than that owned by the taxpayer, failed to follow the mandates of this Court in United States v. Durham Lumber Company, supra and Aquilino v. United States, supra.

Once the Eleventh Circuit found that all the taxpayer held was an equity of redemption, the previous decisions of this Court required that the Government's lien attach only to that equity of redemption. There is no question that prior to the foreclosure, this gave the Government only the right to pay-off the mortgage indebtedness. The question that would then remain is what is the result of the foreclosure upon that equity of redemption.

Relying solely on Trauner v. Lowery, 369 So.2d 531 (Ala. Sup. Ct. 1979), the Eleventh Circuit held that "a complete merger of title resulted" when Petitioners foreclosed without notice to the Government. While Trauner v. Lowery, supra, may bea generalized concept in Alabama, the Eleventh Circuit's reliance on that case alone ignores and

misinterprets the weight of the law with respect tothe doctrine of merger as applied to cases similar to the present. In so doing, the Court misapplied Alabama law.

The applicable rule of law is more precisely stated in Boatwright v. Fennell, 213 Ala. 10, 104 So.1 (1925) wherein the Alabama Supreme Court stated:

> "As a general rule, when the legal and equitable titles become united in the mortgagee, the mortgage is merged by the unity of possession; if, however, 'it is in the interest of the mortgagee to keep the titles distinct, there is no merger, and an intervening right between the mortgage and the equity prevent a merger' [citations omitted] 'If there is any reason for keeping it alive, . . . equity will not destroy' the lien which has been acquired by the holder of legal title." (emphasis added).

In the present case, there exists an intervening interest, to-wit: the Government's lien. In circumstances where there is an intervening junior encumbrance, Alabama law is clear that no merger takes place. When the equity of redemption is purchased by the mortgagee, the mortgage still exists if it is to the mortgagee's interest to protect the mortgagee against additional charges or encumbrances. Burns v. Charles W. Shepard & Co., 231 Ala. 666, 166 So. 416 (1936). Yet, the holding below does exactly the opposite of what the court in Boatwright v. Fennell, supra held; instead of preserving the title so as to protect the rights of the mortgagee, its holding would destroy those rights.

As to the results of a foreclosure without notice, the Alabama Supreme Court has addressed this issue in the analogous

situation of a judicial foreclosure wherein a junior mortgagee is not added as a party.[2] The legislative history of 26 U.S.C. Section 7425 indi-cates that Congress clearly intended just such an analogy, when the Committee on Finance observed:

> Where foreclosures covered by this provision are made without proper notice to the Government, the bill provides that this does not affect the Government's claim under a tax lien (as where the Government is not joined in a judicial foreclosure).

Federal Tax Lien Act of 1966, S.Rep. No. 1708, 89th Cong., 2d Sess., reprinted in

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[2]Prior to Federal Deposit Insurance Corporation v. Morrison, 747 F.2d 610 (11th Cir. 1984) there was no notice requirement to subordinate lienholders in non-judicial foreclosure actions in Alabama, except for the requirements of 26 U.S.C. Section 7425. Accordingly, there is no prior case law dealing with the failure to provide notice in non-judicial foreclosures, while there is established law dealing with the failure to include necessary parties in judicial proceedings as required under previous state law.

1966 U.S. Code Cong. and Ad. News 3722, 3749.

> At common law . . ., if the senior mortgage has been foreclosed by a decree in sale, and the junior mortgagee has not been made a party to a foreclosure suit, he is not barred of his right to redeem. In such case, the junior mortgagee . . ., can file his bill against the purchaser to redeem. This is an equitable right and has nothing to do with our statute of redemption. (emphasis added)

Wiley, Banks and Company v. Ewing, 47 Ala. 418, 424 (1872). The court went on to recognize, at page 426, that, while the senior mortgage had been foreclosed, the junior mortgagee must pay off the whole mortgage debt, with charges and costs, if the senior mortgagee was the purchaser at foreclosure. Likewise, in Capehart v. McGahey, 132 Ala. 334, 31 So. 503 (1902), the Alabama Supreme Court considered the failure to bring a

required party to a foreclosure action, and stated:

> "[T]he only consequence of failing to make it a party would be to leave it with the equity of redemption from the senior mortgagee, or from the defendant, who has succeeded to the title of the senior mortgagee." (emphasis added)

Further, the subordinate lienholders equity of redemption continues as long as its lien is operative, McGowan v. Williams, 241 Ala. 588, 4 So.2d 164, 166 (1941).

In Trauner v. Lowery, supra there was no intervening interest, as there is in the present case, and the Alabama Supreme Court was speaking strictly in terms of a "valid" foreclosure. Here, there has not been a "valid" foreclosure of the Government's equity of redemption. The undisputed facts show that the Government admits that this foreclosure was "ineffectual" against the Government

(R. 112). If the foreclosure was ineffectual, it is invalid.

Since the foreclosure was invalid as to the Government, the Government's equity of redemption continues until otherwise terminated or until the Government exercises its right to pay off the whole mortgage debt, with charges and costs. This is the same right the Government held prior to the foreclosure, and, as held in Wiley, Banks and Company v. Ewing, supra continues after foreclosure. But that is all that is preserved or was ever meant to be preserved.

By holding that a merger exists, the Eleventh Circuit again failed to follow the mandate of this Court. "State law creates legal interests and rights." Morgan v. Commissioner, 309 U.S. 78, 80, 60 S.Ct. 424, 426, 84 L.Ed. 585 (1940).

To determine whether such a state created interest or right has merged as a result of foreclosure, the Court "must look to state law" as required by Aquilino v. United States, supra. (emphasis added)

It is clear that a foreclosure sale without notice to the Government is made "subject to and without disturbing" the Government's lien. The enactment of Section 7425 is a direct result of this Court's holding in United States v. Brosnan, 363 U.S. 237 (1960), wherein the Court adopted as federal law the state law governing the divestiture of tax liens. Under Alabama law, prior to the enactment of Section 7425, a foreclosure without notice to the Government would have extinquished the Government's lien entirely leaving the Government with only a one year statutory right of redemption. Petitioner contends that all Section 7425

does is prevent the Government's lien from being extinquished without proper notice; it does not give the Government a superior right to the fee simple title, thus causing a forfeiture of the senior mortgagee's rights. The property rights are still governed by state law, as this Court has repeatedly held, and Alabama law holds that the Government's rights continue in its equity of redemption.

CONCLUSION

Petitioner's position can best be summarized as follows:

1. The taxpayer's interest in the property is an equitable right of redemption. Federal Deposit Insurance Corp. v. Morrison, supra.

2. The Government's lien under 26 U.S.C. Section 6321 attaches to the

"rights to property . . . belonging to such" taxpayer. Therefore, the Government's lien attaches to the equity of redemption, not the realty itself. The United States Supreme Court, in Aquilino v. United States, supra recognized that the Government's lien only attaches to and is defined by to state created property rights.

3. When Petitioner foreclosed without notice to the Government, the foreclosure was ineffectual and invalid as to the Government's lien. The Government's lien in the equity of redemption was not discharged by such foreclosure. Gilliland v. United States, 47 A.F.T.R. 2d 1364, 81-1 USTC paa. 9322 at 86, 840 (M.D.Tenn.1981).

4. Therefore, the Government's equity of redemption continues after foreclosure. Until otherwise terminated,

this gives the Government the right to pay off the mortgage debt. Burns v. Charles W. Shepard & Co., supra; Wiley, Banks and Company v. Ewing, supra.

5. This right has nothing to do with the Government's statutory right of redemption, which it may have later after a foreclosure which is effectual as to it.

This position gives effect to the letter of Section 7425 as well as the intent of this Section, as expressed in the legislative history. Any other interpretation, and, in particular, that given by the Eleventh Circuit, results in an unconstitutional taking of Petitioner's property without compensation.

SUMMARY OF GROUND FOR ACCEPTING SUPREME COURT REVIEW

A novel question is presented with regard to whether a non- judicial foreclosure, conducted without notice to

the government, results in the complete forefeiture of a mortgagee's interest in the property. This question has not previously been addressed by this Court. The Eleventh Circuit has improperly interpreted 26 U.S.C. Section 7425 in such a way as to cause mortgagees to lose valuable property rights. This can not be the intention of that Code section, and, if it is, then such intent must be unvalid.

Further, the Eleventh Circuit's interpretation of 26 U.S.C. 7425 results in the creation of a property interest in the government which is not recognized by State law. Such a creation of property rights violates this Court's long standing rulings that property rights are only created by State law, U.S. v. Rodgers,51 U.S.L.W. 4261, 83-U.S.T.C. para. 9374 (May 31, 1983); supra;

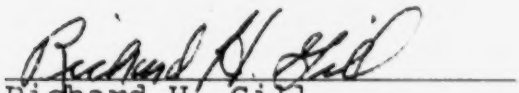
Aquilino v. United States, supra; Morgan v. Commissioner, supra. The Eleventh Circuit's opinion thus creates an unnecessary and illogical conflict between state and federal law. Petitioner's position allows compatibility between state and federal law, gives full meaning to Section 7425 and avoids any conflict between state and federal law and avoids violence to due process considerations under the 5th Amendment.

The Eleventh Circuit's holding goes far beyond this particular case. This ruling, if allowed to stand, will have nationwide application and will effect the stability of land titles across the country.

For these reasons, a writ of certiorari should issue to review and

revise the judgment and opinion of the Eleventh Circuit.

Respectfully submitted,



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Dated: March 3, 1986

EXHIBIT "A"

IN THE UNITED STATES DISTRICT COURT FOR
THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

MID-STATE HOMES, INC.,	)	
Plaintiff	)	CIVIL ACTION NO.
VS.	)	83-AR-1072-S
UNITED STATES OF AMERICA,	)	
Defendant	)	

ORDER

For the reasons set forth in the accompanying Memorandum Opinion, the Court expressly determines that there is no genuine issue as to any material fact and that plaintiff, Mid-State Homes, Inc., is entitled to summary judgment in its favor as a matter of law with respect to certain of its claims for relief, but not as to others which are rendered MOOT. It is therefore

DECLARED, DECREED AND DETERMINED as follows:

1. The interest of plaintiff, Mid-State Homes, Inc., is superior to the interest of defendant, United States of America, as to following described real property situated in Walker County, Alabama, viz:

> A lot or parcel of land situated in the SE 1/4 of the NW 1/4 of Section 17, Township 13 South, Range 8 West, more particularly described as follows: Commence at the SE Corner of the 12 acre tract more or less being known by deed as Lot #3 and being the same property as recorded in Volume 421 at Page 521-24 in the Probate Office of Walker County, Alabama, thence run S 88 deg. 00 min. W along the North side of a County Gravel Road for a distance of 190.0' feet to the point of beginning, thence continue along same line for a distance of 105.0' feet, thence run N 1 deg. 45 min. W and parallel to the East line of said 12 acre tract for a distance of 210.0' feet, thence run N 88 deg E and parallel to said road for a distance of 105.0' feet, thence run S 1 deg. 45 min. E for a distance

of 210.0' feet to the point of beginning.

2. Plaintiff's foreclosure of November 30, 1982, was valid and was effective to cut off defendant's tax lien, subject to its right to redeem.

3. Defendant's right to redeem has not been extinguished, and it shall have the right to redeem by paying to plaintiff the sum appropriate to effect redemption under 26 U.S.C. Sec. 7425(d)(2), 28 U.S.C. Sec. 2410(d) and Sec. 6-5-234, Code of Alabama (1975), within 30 days of this date. If defendant does not so redeem, defendant shall vacate the above described property within 10 days thereafter and deliver possession to plaintiff.

4. All relief not expressly granted hereinabove is DENIED.

5. Each party shall bear its own costs.

DONE this 23rd day of May, 1984.

/s/ William M. Acker, Jr.
WILLIAM M. ACKER, JR.
UNITED STATES DISTRICT
JUDGE

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

MID-STATE HOMES, INC.,	)	
Plaintiff	)	CIVIL ACTION NO.
VS.	)	83-AR-1072-S
UNITED STATES OF AMERICA,	)	
Defendant	)	

MEMORANDUM OPINION

On April 12, 1984, this Court, of its own motion, entered an Order deferring ruling on the motion of plaintiff, Mid-State Homes, Inc. (Mid-State) for summary judgment pending a decision by defendant, United States of America (U.S.A.) as to whether or not it will press its appeal now pending in the Circuit Court of Appeals for the Eleventh Circuit in Southern Bank of Lauderdale County v. Internal Revenue Service, et al., CV 82-HM-5236-NW, 84-1 U.S.T.C.

para. 9245 (N.D.Ala.1984). Upon reflection, and because U.S.A. remains in possession of the real property here involved, the Court now concludes that there is no good reason for further delay, especially inasmuch as U.S.A. has conceded that the basic legal questions are identical in this case and in Southern Bank.

THE CONTROLLING FACTS

The controlling undisputed facts, relied upon in support of Mid-State's motion for summary judgment, are these:

1. On October 2, 1972, the Fergusons, who then owned the real property here involved, executed a first mortgage to Jim Walter Homes, Inc. The mortgage was duly recorded.

2. On November 5, 1979, U.S.A. filed a tax assessment against the

Fergusons pursuant to 26 U.S.C. Section 6321.

3. On July 17, 1980, U.S.A. filed a notice of federal tax lien against the taxpayers pursuant to 26 U.S.C. Section 6323 in the amount of $8,580.18, meaning that the tax lien attached as of November 5, 1979.

4. On December 20, 1981, the mortgage was assigned to Jim Walter Homes, Inc., to Mid-State.

5. The fergusons defaulted in their mortgage payments.

6. On December 30, 1981, Mid-State foreclosed pursuant to its power of sale but without giving notice to U.S.A. pursuant to 26 U.S.C. Section 7425. Its foreclosure deed was recorded on March 15, 1982.

7. Recognizing that its foreclosure was ineffectual as against U.S.A. because

of lack of notice, Mid-State again foreclosed on November 30, 1982, but this time after giving proper notice to U.S.A. pursuant to 26 U.S.C. Section 7425. Mid-State became the purchaser at the said foreclosure sale after making the highest and best bid, and recorded its foreclosure deed on December 9, 1982.

8. On April 22, 1983, U.S.A. took possession of and still maintains possession of the Ferguson property.

9. By agreement between the parties U.S.A. has agreed not to convey or to otherwise dispose of the Ferguson property until a final adjudication in this case.

10. The parties have agreed that this Court has jurisdiction to declare the respective interests of the parties in the Ferguson property.

THE APPLICABLE LAW

It is obvious that U.S.A. relies on Baldwin County Savings Bank and Loan Ass'n. v. United States, 81-2 U.S.T.C. para. 9619 (S.D.Ala.1981), while Mid-State relies on Southern Bank, supra., which was decided on February 16, 1984, long after the transactions here being scrutinized and after the above entitled action was filed.

This Court has not changed its mind since it wrote Southern Bank, and therefore believes that Mid-State's second foreclosure was successful in cutting off U.S.A.'s tax lien, leaving U.S.A. with no more than a lien creditor's statutory right to redeem. According to Mid-State's motion for summary judgment it has abandoned any claim for damages, but whether it has intentially abandoned such claim or not, the Court cannot conclude

that U.S.A.'s seizure exposed it to liability in light of its understandable reliance upon Baldwin County, supra. Furthermore, although the statutory right to redeem provided by Section 6-5-230, Code of Alabama (1975) is, on its face, one year, and more than one year has elapsed since Mid-State's second foreclosure, without any formal attempt to redeem, there are facts here upon which equitable principles mandate an extension of U.S.A.'s right to redeem. First, it was not unreasonable for U.S.A. to rely on what the Court said in Baldwin County. It was not required to predict Southern Bank. Secondly, U.S.A. is in actual possession of the subject property and has not purported to convey the property because it agreed with Mid-State not to do so. Mid-State is estopped to deny some residual property interest in U.S.A.

It would be as unconscionable in this case to take away U.S.A.'s right to redeem as this Court found it would have been in Southern Bank to take away from Southern Bank its firt mortgage lien. The circumstances here force an application of a reverse laches. Thirdly, this litigation began while the one year right to redeem was still outstanding, so that the pendency of the suit automatically extended the right to redeem. The Supreme Court of Alabama in Dunn v. Ponceler, 235 Ala. 269, 178 So. 40, 46 (1938) stated the applicable principle thusly:

> In Amer. and Eng. Encl. of Law, it is broadly stated in the text that if the matter in dispute between the parties has, during the time when the delay occurred, been the subject of litigation, the plaintiff's delay is sufficiently excused.

The analogy to a suit to redeem is obvious. Certainly a purchaser at foreclosure sale who insists that a particular claimant has no right to redeem and who forces the matter to court before the period of redemption expires cannot thereafter be heard to complain that the would-be redemptioner did not redeem on time.

Another Alabama decision which the Court finds persuasive is the more recent Caudle v. First Federal S & L Ass'n. of Sylacauga, 327 So.2d 911 (Ala.1975). There the Supreme Court of Alabama applied general principles of equity in order to extend the statutory right to redeem beyond its precise limitation period. It cited not only Dunn v. Ponceler, supra., but First National Bank of Opp v. Wise, 235 Ala. 124, 177 So. 636 (1937), and concluded that under special

circumstances it would be "unjust and unreasonable" to enforce the redemption period strictly. This Court concludes that to apply the one year period strictly to U.S.A. under the instant circumstances would be just as "unjust and unreasonable" as it would have been in Caudle, if not more so.

Other applicable maxims of equity jurisprudence are: (1) He who seeks equity must do equity; (2) Equity will not suffer a wrong without a remedy; (3) Equity imputes an intent to fulfill an obligation; and (4) Equity is a court of conscience. These principles are no more than expressions which were reflected directly or indirectly in the Alabama cases above cited.

Based on the conclusions which this Court has reached there is no necessity for expressing an opinion on the question

of the constitutionality of 26 U.S.C. Section 7425 or an opinion on the alleged failue of U.S.A. to comply with 26 U.S.C. Section 6331(a). These issues are mooted by the rationale of this Court.

In order to recognized U.S.A."s right to redeem, the Court will in its accompanying Order grant U.S.A. 30 days within which to redeem from Mid-State or to deliver possession within 10 days thereafter.

An appropriate separate order will be entered.

DONE this 23rd day of may, 1984.

/s/ William M. Acker, Jr.
WILLIAM M. ACKER, JR.
UNITED STATES DISTRICT JUDGE

EXHIBIT "B"

IN THE UNITED STATE DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
NORTHWESTERN DIVISION

SOUTHERN BANK OF LAUDERDALE COUNTY,	)	
Plaintiff	)	NO. CV 82-HM-
VS.	)	5236-NW
INTERNAL REVENUE SERVICE, UNITED STATES OF AMERICA,	)	
Defendant	)	

ORDER

The above entitled civil action came on to be heard at a scheduled motion docket of this court held at the Federal Courthouse in Florence, Alabama on Wednesday, January 25, 1984 commencing at 1:30 p.m., upon motion of defendant Internal Revenue Service, United States of America (IRS) for summary judgment in its favor with respect to the declaratory relief prayed for in the complaint and

upon motion of plaintiff Southern Bank of Lauderdale County (Bank) for summary judgment in its favor with respect to the declaratory relief prayed for in its complaint.

Having considered the motions for summary judgment, the evidentiary matter offered in support thereof and in opposition thereto, the pleadings, the written briefs and oral argument, and applicable law, the court expressly determines that there is no genuine issue as to any material fact, and that plaintiff is entitled to declaratory judgment in its favor as a matter of law with respect to some of the relief prayed for in its complaint. Accordingly, in conformity with the Memorandum of Decision entered contemporaneously herewith, it is

ORDERED, ADJUDGED and DECREED that plaintiff's motion for summary judgment

in its favor against defendant for the relief prayed for in plaintiff's complaint as hereinafter set forth is GRANTED and that judgment be and the same hereby is ENTERED in favor of plaintiff Bank and against defendant IRS.

It is further ORDERED, ADJUDGED and DECREED that the nonjudicial foreclosure sale conducted by Bank on March 30, 1982 involving a parcel of real property in Lauderdale County, Alabama more specifically described as:

> Lot 39, Riverchase, a subdivision in Lauderdale County, Alabama, according to the plat thereof as recorded in the Office of the Judge of Probate of said County in Plat Book 5, Pages 31-32,

was made without proper notice to defendant IRS, lienor, as is required by I.R.C. Section 7425(b)(1) and was, as to IRS, a nullity as a matter of law.[1]

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[1]The effectiveness of this nonjudicial foreclosure sale as to any interested

It is further ORDERED, ADJUDGED and DECLARED that Bank, by virtue of its two mortgages duly recorded in the Office of the Judge of Probate of Lauderdale County, Alabama on November 30, 1978 and April 18, 1979, despite the foreclosure sale, retains a lien upon the property in issue, more specifically described above, that is superior to the federal tax lien of defendant IRS upon said property, notice of which was filed by IRS in the Office of the Judge of Probate of Lauderdale County, Alabama on February 5, 1982. The Court denies all relief requested except as above granted. The Court will not give the parties advice as to what their future action should be to protect their respective interests, but

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parties who were not joined in this lawsuit is an issue that this court need not presently address.

simply determines their respective present positions as to the subject real property.

It is further ORDERED that IRS's counterclaim is hereby DISMISSED.

It is further ORDERED that each party shall bear its own costs.

DONE and ORDERED this 14th day of February, 1984.

/s/ William M. Acker, Jr.
United States District
Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
NORTHWESTERN DIVISION

SOUTHERN BANK OF LAUDERDALE COUNTY,	)	
Plaintiff	)	NO. CV 82-HM-5236-NW
VS.	)	
INTERNAL REVENUE SERVICE, UNITED STATES OF AMERICA,	)	
Defendant	)	

MEMORANDUM OF DECISION

Plaintiff Southern Bank of Lauderdale County (hereinafter "Bank") brought this action seeking to quiet title to a certain parcel of improved real property located in Lauderdale County, Alabama (hereinafter "property"). The property was originally owned by Florence Reinforced Plastics, Inc. (hereinafter "Plastics"), an Alabama corporation. Plastics executed two mortgages on the property to Bank. These mortgages

were properly recorded by Bank in the Office of the Judge of Probate in Lauderdale County, Alabama on November 30, 1978 and April 18, 1979. Defendant and counterclaimant Internal Revenue Service, United States of America (hereinafter "IRS"), claimed a lien on the property based upon Plastics' unpaid federal employment and withholding tax liabilities, penalties and interest. It is uncontested that IRS gave Plastics proper notice of the tax deficiencies, made proper demand for payment and on February 5, 1982 filed a Notice of Federal Tax Lien in the Office of the Judge of Probate in Lauderdale County, Alabama. Plastics defaulted on the mortgages and on March 30, 1982 Bank conducted a non-judicial foreclosure sale pursuant to the power of sale contained in the mortgage. Although this sale was

advertised in the Florence Times, it was stipulated by Bank in its own complaint that no notice was provided to IRS as is required by I.R.C. Section 7425(b)(1)[1] and no prior consent for the sale was obtained from IRS. Bank bought the property at this non-judicial foreclosure sale for $37,714.18.

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[1]Section 7425(b)(1) provides in pertinent part:

> [A] sale of property on which the United States has or claims a lien, or a title derived from enforcement of a lien, under the provisions of this title, made pursuant to an instrument creating a lien on such property, pursuant to a confession of judgment on the obligation secured by such an instrument, or pursuant to an non-judicial sale under a statutory lien on such property --
>
> > (1) shall, except as otherwise provided, be made subject to and without disturbing such lien or title, if notice of such lien was filed or such title recorded in the place provided by law for such filing or recording more than 30 days before such sale and the United States is not given notice of such sale in the manner prescribed in subsection (c)(1); . . .

In the complaint, Bank seeks: (1) an injunction prohibiting IRS from selling the property, (2) a discharge of the lien of IRS under terms of substitution of the proceeds from the sale or a posting of a bond as provided by 28 U.S.C. Section 6325, and (3) the court's determination that Bank owns the property with the rights of IRS or any other interested party being governed by redemption provisions of state law. Bank also filed a motion for a preliminary injunction which was later withdrawn. On June 30, 1982, IRS filed an answer and a counterclaim wherein prayer was made for the court to: (1) decree that IRS had a valid encumbrance on the property, (2) order a sale of the property pursuant to I.R.C. Section 7402(c), and (3) award IRS it costs.

On April 19, 1983 IRS filed a motion for summary judgment; Bank filed a motion for summary judgment on May 25, 1983. Both parties filed briefs in support of their respective summary judgment motions.

It is Bank's position that the lien of IRS for taxes under I.R.C. Section 6321 would only apply to the interest in the property that Plastics (taxpayer) held during the time prior to the foreclosure sale. Section 6321 provides:

> If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property whether real or pesonal, belonging to such person.

Bank asserts that state law controls in determining what legal interest Plastics

had in the property while federal law determines whether a lien attached to the property and the priority of competing liens asserted against the property. IRS does not seem to quarrel with this general proposition. Due to the fact Alabama is a "title" state--i.e., upon execution of a mortgage legal title passes to the mortgagee--Bank asserts that the only interest retained by Plastics was an equitable right of redemption. Bank thus argues that Plastics equitable right of redemption was the only interest to which IRS's tax lien could have attached. The court finds merit in this argument. Although a foreclosure sale generally extinguishes the equitable right of redemption, it is the position of both parties that because IRS did not receive notice of the sale, the tax lien remained in effect; the

parties do differ, however, as to what property or property interest the lien of IRS attached. Bank would thus have the court determine that IRS presently retains a statutory right to redeem while Bank, as purchaser at the foreclosure sale, holds legal title. IRS would have the court determine that its lien attached to the property prior to the foreclosure sale and remained attached to the property after the foreclosure sale free of the Bank's lien.

IRS relies upon Baldwin County Savings and Loan Association v. United States, 81-2 U.S.T.C., para. 9619 (S.D.Ala.1981). Although Baldwin County involved facts that are essentially the same as the facts in the above entitled civil action, this court respectfully disagrees with the approach taken therein by the Honorable W. B. Hand, United

States District Judge of the Southern District of Alabama. In Baldwin County, as in the case presently before the court, plaintiff-mortgagee nonjudicially foreclosed its mortgage without notifying the United States who had filed a Notice of Federal Tax Lien against mortgagor more than 30 days prior to the foreclosure sale. The court in Baldwin County held that: (1) due to the lack of notice to United States the lien of United States was undisturbed by the foreclosure sale; (2) the mortgage was extinguished by the sale; and (3) the junior lien of the United States was automatically elevated to senior lien status.

This court believes that the argument of IRS, which is based upon Baldwin County, contains an inconsistency. This inconsistency, which is crucial in this court's determination, concerns the legal

effect IRS would have this court give the nonjudicial foreclosure sale conducted by Bank on March 30, 1982. Either the foreclosure sale is effective as to IRS, or it is not. IRS cannot call the sale effective as to the rights of Bank and yet call it effective to give IRS a first lien. The law cannot allow such an anomoly. Equity and fairness preclude IRS from "having its cake and eating it too" just because of error of notice. It seems to this court that Bank not only has the better equitable argument, but the better technical argument. In Traunder v. Lowrey, 369 So.2d 531 (Ala.1979), the Supreme Court of Alabama reaffirmed the principle that an Alabama mortgagee has the legal title and that a mortgagor can only convey his equity of redemption. Thus, the IRS lien could only attach to what the mortgagor had and

could not leap ahead of Bank simply because Bank purchased at foreclosure. It would be unfair in the extreme to make a distinction here between foreclosure sales where a third party purchases and where the mortgagee purchase. The court must therefore conclude that, as to IRS, the nonjudicial foreclosure sale conducted by Bank on March 30, 1982 is a nullity. Legal title to the property in issue under the law of Alabama was held by Bank prior to the sale and continues to be held by Bank. The effect of this court's ruling is to place the parties in the same position vis-a-vis each other as they were in just prior to Bank's nonjudicial foreclosure sale. This means, of course, that the court disagrees with the Bank's contention that IRS only has a statutory right to redeem.

A separate order implementing the provisions of this Memorandum of Decision will be entered contemporaneously herewith.

DONE this 14th day of February, 1984.

/s/ William M. Acker, Jr.
United States District
Judge

EXHIBIT "C"

SOUTHERN BANK OF LAUDERDALE COUNTY,
Plaintiff-Appellee,

v.

INTERNAL REVENUE SERVICE,
United States of America,
Defendants-Appellants,

MID-STATE HOMES, INC.,
Plaintiff-Appellee,

v.

UNITED STATES of America,
Defendant-Appellant.

Nos. 84-7280, 84-7501.

United States Court of Appeals,
Eleventh Circuit.

Sept. 13, 1985.

Mortgagee which conducted nonjudicial foreclosure sale and purchased property without providing notice to Government, which had filed tax liens against mortgagors, brought action to quiet title to property as against Government. The United States District

Court for the Northern District of Alabama, William M. Acker, Jr., J., 586 F.Supp. 12, held mortgagee's lien superior to federal tax liens, and Government appealed. On consolidated consideration with similar case, the Court of Appeals, Clark, Circuit Judge, held that failure of mortgagees to give statutory notice to Government before they conducted foreclosure sales and purchased property caused their mortgage liens to be extinguished and federal tax liens to be elevated from their junior status.

Reversed and remanded.

1. Internal Revenue 4792

Where Government filed notice of tax liens at least 30 days prior to foreclosure sales and mortgagees did not provide Government with statutory notice of

sales, sales of property to mortgagees were made subject to and without disturbing federal tax liens; failure of mortgagees to provide notice to Government before they conducted foreclosure sales and purchased property caused their mortgage liens to be extinguished and federal tax liens to be elevated from their junior status. 26 U.S.C.A. Section 7425.

2. Internal Revenue 4777

Mortgagors who held equitable right of redemption in mortgaged property under Alabama law, so as to be possessed of legal title against all the world except mortgagee or its assigness, had "property" to which federal tax lien could attach. 26 U.S.C.A. Section 6321.

See publication Words and Phrases for other judicial constructions and definitions.

Appeals from the United States District Court for the Northern District of Alabama.

Before KRAVITCH and CLARK, Circuit Judges, and WRIGHT*, Senior Circuit Judge.

CLARK, Circuit Judge:

These two cases which were consolidated for oral argument purposes, present questions about the federal tax lien and the notice provisions of 26 U.S.C. Section 7425(b). In both cases the district court granted summary judgment in favor of the appellees Southern Bank of

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*Honorable Eugene A. Wright, U.S. Circuit Judge for the Ninth Circuit, sitting by designation.

Lauderdale County (Southern Bank) and Mid-State Homes, Inc. (Mid-State). For the reasons discussed below, we reverse.

I. FACTS

The facts in both cases are undisputed. The appellees, Southern Bank and Mid-State, obtained their respective interests in the property by either the assignment or execution of mortgages upon which the taxpayers were obligated.[1] These mortgages were properly recorded.

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[1]In Southern Bank of Lauderdale County v. Internal Revenue Services, United States of America, 586 F.Supp. 12 (N.D.Ala.1984) [hereinafter cited as Southern Bank], the taxpayer, Florence Reinforced Plastics, Inc., an Alabama Corporation, executed two mortgages to Southern Bank on a parcel of real property located in Lauderdale County, Alabama.

In Mid-State Homes, Inc. v. United States, No. 83-AR-1072-S, slip op. (N.D.Ala. May 22, 1984) [hereinafter cited as Mid-State], the taxpayers, the Fergusons, executed a first mortgage to Jim Walters Homes, Inc. who later assigned the mortgage to Mid-State.

Thereafter, the Internal Revenue Service (IRS) made assessments against the taxpayers for unpaid taxes and properly filed notices of the federal tax liens pursuant to 26 U.S.C. Section 6323.[2]

The taxpayers defaulted on their mortgages. Thereafter, Southern Bank and Mid-State conducted nonjudicial foreclosure sales in accordance with the power of sale contained in the mortgages. Both Southern Bank and Mid-State admit that they did not provide the United States with notice of the sales as set forth under 26 U.S.C. Section 7425. Nor did the United States consent to the sales.[3] Southern Bank and Mid-State

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[2]In Southern Bank, the taxpayer was assessed $19,025.61. In Mid-State, the taxpayers were assessed $8,580.18.

[3]Under 26 U.S.C. Section 7425(c)(1), notice of a non-judicial or other sale of property "shall be given in writing, by registered or certified mail or by personal service, not less than 25 days prior to such sale, to the Secretary."

were the purchasers of the property at the nonjudicial sales.[4]

Recognizing that its initial foreclosure was ineffectual against the United States because of its failure to give notice, Mid-State foreclosed on the property approximately eleven months after the first foreclosure sale.[5] On this second occasion, however, Mid-State gave proper notice of the foreclosure sale to the United States pursuant to 26

The statute further provides that a nonjudicial or other sale of property "shall discharge or divest such property of the lien or title of the United States if the United States consents to the sale of such property free of such lien or title." 26 U.S.C. Section 7425(c)(2).

[4]Southern Bank purchased the property at the nonjudicial foreclosure sale of $27,714.18. Southern Bank, 586 F.Supp. at 13. Mid-State purchased the property at the nonjudicial sale for $12,542.74. Record, No. 84-7501 at 109.

[5]The first sale was held on December 30, 1981. The second sale was held November 30, 1982. Id. at 112.

U.S.C. Section 7425. Mid-State was the purchaser of the property at this second sale and thereafter recorded its foreclosure deed.

II. PROCEEDINGS IN THE DISTRICT COURT AND ARGUMENTS ON APPEAL

A. Southern Bank

Southern Bank filed its complaint seeking: (1) to quiet title to the property; (2) an injunction prohibiting the IRS from selling the property under its notice of levy; (3) a discharge of the tax lien; and (4) a determination that Southern Bank was the owner of the property with the rights of the IRS or any other interested party to be governed by the redemption provisions of the Code of Alabama.[6] Record, No. 84-7280 at 3, 6.

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[6]See Ala.Code Section 6-5-230 to Section 6-5-246 (1977).

Southern Bank argues that under 26 U.S.C. Section 6321 the tax lien only applied to the interest the taxpayer held in the property prior to the foreclosure sale, that state law controlled the legal interest the taxpayer held in the property, and that federal law limited the tax lien to only that property interest. Because Alabama is a "title" state, which means that legal title passes to the mortgagee upon execution of the mortgage, Southern Bank argues that the only interest retained by the taxpayer prior to foreclosure was its equitable right of redemption. Thus, the tax lien only attached to this equitable right of the taxpayer, which was a right the taxpayer had to gain legal title by paying off the note secured by the mortgage. According to Southern Bank, the government's interest in the property,

subsequent to the foreclosure sale, was only a statutory right of redemption.[7] Southern Bank concedes that because notice of the sale was not given to the IRS, the tax lien remained in effect to that extent.

The United States maintains that due to its lack of notice of the sale, its lien was undisturbed by the foreclosure. Because the sale extinguished Southern Bank's mortgage, the United States contends that its junior lien was automatically elevated to a first lien against the real estate acquired by the purchaser at the sale.

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[7]Southern Bank reaches this conclusion because it held legal title before and after the foreclosure sale and the foreclosure eliminated the mortgagor's right of equitable redemption. The mortgagor then only had a statutory right of redemption. Southern Bank, 586 F.Supp. at 13. See infra at Section III C for a discussion of this issue.

The district court concluded that Southern Bank had a better equitable and legal argument. The court observed:

> Thus, the IRS lien could only attach to what the mortgagor had and could not leap ahead of Bank simply because Bank purchased at foreclosure. It would be unfair in the extreme to make a distinction here between foreclosure sales where a third party purchases and where the mortgagee purchases. The court must therefore conclude that, as to IRS, the nonjudicial foreclosure sale conducted by Bank on March 30, 1982 is a nullity. Legal title to the property in issue under the law of Alabama was held by Bank prior to the sale and continues to be held by Bank. The effect of this court's ruling is to place the parties in the same position vis-a-vis each other as they were in just prior to Bank's nonjudicial foreclosure sale. This means, of course, that the court disagrees with the Bank's contention that IRS only has a statutory right to redeem.

Southern Bank, 586 F.Supp. at 14 (emphasis in original).

B. Mid-State

Because the United States levided and seized possession of the subject

property, Mid-State filed its complaint alleging that the United States wrongfully levied upon the property. Mid-State argues that 26 U.S.C. Section 7425 was unconstitutional as written or applied and that the procedures required under the statute had not been followed. Mid-State sought to enjoin the United States from enforcing its lien and sought to have the subject property returned. Record, No. 84-7501 at 32.

In finding in favor of Mid-State the court stated:

> This Court has not changed its mind since it wrote Southern Bank, and therefore believes that Mid-State's second foreclosure was successful in cutting off U.S.A.'s tax lien, leaving U.S.A. with no more than a lien creditor's statutory right to redeem.
>
> . . .
>
> Based on the conclusions which this Court has reached there is no necessity for expressing an opinion on the question of the constitutionality of 26 U.S.C. Section 7425 or an opinion on the alleged failure of

> U.S.A. to comply with 26 U.S.C. Section 6331(a). These issues are mooted by the rationale of this Court.
>
> Record, No. 84-7501 at 113, 114.

C. Arguments on Appeal

The parties raise similar arguments on appeal. The United States essentially argues that the district court erred when it concluded that "where a nonjudicial foreclosure sale was held without notice to the United States, the sale was a nullity insofar as the Government was concerned and the foreclosing mortgagee consequently retained a lien against the property that was superior to the federal tax liens." Appellant's Brief, No. 84-7501 at 8. It further contends that in Mid-State the district court erred when it treated the second sale as effective to extinguish the federal tax lien on the basis of its holding in Southern Bank. The United States takes the position that

the court's holdings are contrary to the plain language of the statute, its interpretation by the courts, and its legislative history.

Southern Bank admits in its brief:

> A federal tax lien attaches to the taxpayer's interest in property and becomes enforceable against the property whether his interests are extensive or limited. IRS also correctly asserts that state law controls in determining what interest the taxpayer has in the property, and that federal law determines whether a lien attached to the property and the priority of competing liens. Aquilino v. United States, 363 U.S. 509, 80 S.Ct. 1277, 4 L.Ed.2d 1365 (1960); United States v. Brosnan, 363 U.S. 237, 80 S.Ct. 1108, 4 L.Ed.2d 1192 (1960); United States v. Bess, 357 U.S. 51, 78 S.Ct. 1054, 2 L.Ed.2d 1135 (1958). There is no controversy as to these statements of law.

Appellee's Brief, No. 84-7280 at 5.

The appellees argue that 26 U.S.C. Section 7425 was only designed to protect the government's interest in property prior to a nonjudicial foreclosure if the I.R.S. was not given notice of the sale

and that the protection continued because the I.R.S. lien remained after the sale as a lien junior to that of each appellee's lien. They urge that a failure to give notice should not create a "wind fall" or greater interest in the property than the United States held prior to foreclosure. Mid-State points out that "[t]here is nothing in the language of the statute or the legislative hsitory [sic] to suggest that Congress intended to leapfrog priorities. Instead, the clear directive of the statute is simply that the tax lien continues if notice of foreclosure is not given." Appellee's Brief, No. 84-7501 at 5. Both Mid-State and Southern Bank claim that under Alabama law the taxpayers only held an equitable right of redemption, and that this was the only interest to which the tax lien could attach. Thus, it is

argued that to obtain title to the property the IRS must first make payment in full of the prior mortgage indebtedness. The appellees contend that if the government had been given notice before the foreclosue sales, it would have had to purchase the property at foreclosure for the full amount owed to each mortgagee in order to protect the tax lien and obtain any revenue for the government. To change the priorities because of lack of notice, it is urged, would be against the principles of equity and fairness. It is apparent the district court was persuaded by these arguments. We now address the issues raised by this appeal.

III. DISCUSSION

A. Failue of a Mortgagee to Provide Notice of a Nonjudicial Foreclosure Sale Pursuant to 26 U.S.C. Section 7425.

When a taxpayer, who is liable to pay any tax, neglects or refuses to pay

the tax after demand, the amount becomes "a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person." 26 U.S.C. Section 6321.[8] The overriding purpose of the tax lien statute obviously is to ensure prompt revenue collection." United States v. Kimbell Foods, Inc., 440 U.S. 715, 734-35, 99 S.Ct. 1448, 1462, 59 L.Ed.2d 711 (1979). As we observed in United States v. Second National Bank of North Miami,

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[8]The statute provides:

> If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.
>
> 26 U.S.C. Section 6321 (emphasis added).

502 F.2d 535 (5th Cir.1974), cert. denied, 421 U.S. 912, 95 S.Ct. 1567, 43 L.Ed.2d 777 (1975), "[i]t has long been recognized that liens to guarantee payment of taxes are an important element of the sovereign's taxing power." Id. at 545. With these objectives in mind, we must rule on the questions presented in this appeal. We initially determine the consequences that arise when a mortgagee fails to provide notice to the government of a foreclosure sale and subsequently purchases property that is subject to a valid federal tax lien.

Under 26 U.S.C. Section 7425(b) "a sale of property on which the United States has or claims a lien ... shall ... be made subject to and without disturbing such lien or title, if notice of such lien was filed or such title recorded in the place provided by law for such filing

or recording more than 30 days before such sale and the United States is not govern notice of such sale in the manner prescribed in subsection (c)(1)..." Id. The statute sets forth two requirements that must exist before a sale of property, upon which the United States has a tax lien, can be made subject to the lien. First, the United States must file its notice of lien 30 days prior to the sale. Second, the United States must not be furnished with notice of the sale in the time and manner prescribed by 26 U.S.C. Section 7425(c)(1). One commentator, in discussing these notice provisions, made the following observation:

> The judicial or nonjudicial procedures provided under local law by which the holder of a senior mortgage or other lien may foreclose the interests of the debtor and of junior lienors may not suffice to extinguish a junior federal lien, unless the senior lienor complies with the further requirements prescribed by Congress for the protection of the Government.

Plumb, Federal Liens and Priorities Agenda for the Next Decade III, 77 Yale L.J. 1104, 1168 (1968) emphasis in original.

[1] We have determined that the liens attached to the property in question.[9] It is undisputed that the government filed notice of the tax liens at least 30 days prior to the foreclosure sale. It is also undisputed that the mortgagees, Southern Bank and Mid-State, did not provide the government with notice of the sales pursuant to 26 U.S.C. Section 7425(c). Since both of the requirements for a sale to be made subject to the tax lien have occurred in these cases, we hold that the sales of the property subject to the tax liens

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[9]See infra at Section III C.

were made subject to and without disturbing the federal tax liens.[10]

Our conclusion is supported by Myers v. United States, 647 F.2d 591 (5th Cir. Unit A 1981).[11] In Myers, the mortgagee held the senior encumbrance on the property. The tax lien, which was duly recorded, was junior to the mortgage. After the tax lien was filed a sheriff's sale was held pursuant to a nonjudicial foreclosure proceeding initiated by the mortgagee and the mortgagee purchased the

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[10]Mid-State agrees that the property is "subject to" the federal tax lien. However, it argues that it has legal title to the property "subject to" the government's statutory right of redemption. As we shall demonstrate in the following sections of this opinion, this argument is without merit.

[11]In Bonner v. City of Prichard, 661 F.2d 1206 (11th Cir.1981) (en banc), this court adopted as binding precedent all of the decisions of the former Fifth Circuit handed down prior to the close of business on September 30, 1981. Id at 1209.

property. The mortgagee subsequently sold the property to Myers, a third party. At no time during the foreclosure proceedings was the United States joinded as a party or served with notice of the sale. The government levied on the property and served Myers with a notice of the seizure. Myers brought an action for wrongful levy.

In deciding that the tax lien was not discharged by the nonjudicial foreclosure sale because of the mortgagee's failure to give notice, we observed that 26 U.S. C. Section 7425 "was intended to protect the United States, where its tax lien is junior, from its discharge under state law without prior notice to the United States of proceedings by which the property is sold." Id. at 596. We concluded that:

> Section 7425(b) provides that where notice of a federal tax lien is duly filed more than thirty days prior to

> the date of the foreclosure sale, the sale will be made subject to the federal lien unless written notice of the sale is served upon the United States at least twenty-five days before the sale is held. It is undisputed that such notice was not given in the present case. It therefore follows that the second federal lien was not discharged by the foreclosure sale.

Id. at 601.

In Little v. United States, 704 F2d 1100 (9th Cir.1983), the Ninth Circuit reached a similar conclusion. The court observed that "[s]ection 7425(b) expressly provides that a nonjudicial sale of property on which the United States has a lien ... shall be made 'subject to and without disturbing such lien or title' if the United States is not given notice of such sale in the manner presecribed in subsection (c)(1)." Id. at 1107 (emphasis in original) (footnote omitted).[12]

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[12]Another case that is consistent with our position is Baldwin County Savings & Loan Association v. United States, 81-2 Tax Ct.Rep. (CCH) Para. 9619

And, in United States v. Rodgers, 461 U.S. 677, 103 S.Ct. 2132, 76 L.Ed.2d 236 (1983), the Court noted that "[o]nce a lien has attached to an interest in

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(S.D.Ala.1981). In Baldwin, the taxpayer executed a mortgage in favor of the plaintiff/mortgagee. The mortgage was duly recorded. The United States subsequently filed a notice of federal tax liens against the taxpayer. The mortgagee, without providing notice pursuant to 26 U.S.C. Section 7425, conducted a nonjudicial foreclosure sale. The mortgagee purchased the property at the sale.

The district court found that the tax liens attached to the real property in issue. It concluded that because the United States was not given notice of the sale, the federal tax liens were not discharged. Thus, the court held that "by purchasing the property for an amount equal to the unpaid balance of the promissory note, not only was the mortgage extinguished, but also the debt was paid. Accordingly, the tax liens on the subject real property were promoted to a senior lien status, and that is the position they enjoy today." Id. at 88,065.

Neither appellee attempts to distinguish Myers, by which we are bound, nor Little, by which we are not bound, but which we find persuasive.

property, the lien cannot be extinguished (assuming proper filing and the like) simply by transfer or conveyance of the interest." Id. at 2141 n. 16.

B. Elevation of the Federal Tax Lien From its Junior Status

Southern Bank and Mid-State argue that to allow the government to summarily levy on the property would allow it to "leapfrog priorities." Their contention is that this would cause an inequitable result for it would put the government in a better position than prior to the foreclosures.

These arguments relate to the priority and overall operation of the federal tax lien law. It is established that matters directly affecting the nature and operation of the federal tax lien and its relative priority present federal questions. See United States v. Brosnan, 363 U.S. 237, 240, 80 S.Ct. 1108, 1110,

4 L.Ed.2d 1192 (1960) ("[M]atters directly affecting the nature or operation [of federal tax liens] are federal questions, regardless of whether the federal statutory scheme specifically deals with them or not."); Aquilino v. United States, 363 U.S. 509, 513-14, 80 S.Ct. 1277, 1280, 4 L.Ed.2d 1365 (1960) ("[O]nce the tax lien has attached to the taxpayer's state-created interests, we enter the province of federal law, which we have consistently held determines the priority of competing liens asserted against the taxpayer's 'property' or 'rights to property.'").

With this principle in mind, we address the appellee's arguments. The federal tax lien has been elevated to its current status because of the principles regarding merger and foreclosure sales and due to the operation of 26 U.S.C.

Section 7425. When a mortgagee forecloses on property, the doctrine of merger generally operates to extinguish the mortgage indebtedness and the lien held by the mortgagee. "In other words, the mortgage is no longer in existence, and thus the original holder of the mortgage no longer has a mortgage lien which can be foreclosed a second time, even if the original indebtedness is not satisfied from the sales proceeds." Baldwin County Savings & Loan Assoc. v. United States, 81-2 USTC Para. 9619 at 88,065 (S.D.Ala.1981). "The equity of redemption in either case, however, is extinguished by a valid foreclosure sale ..." Trauner v. Lowrey, 369 So.2d 531, 534 (Ala.Sup.Ct.1979).

Because Southern Bank and Mid-State conducted the foreclosure sales and purchased the subject property it is

reasonable for us to conclude that a complete merger of title resulted, vesting the fee simple title to the property in the mortgagees. This title is superior to all liens except those not extinguished, such as state, county and city taxes, a federal tax lien properly perfected as in this case, and such other liens as federal and local governments may determine are not extinguishable by a nonjudicial foreclosure sale.[13] For

---

[13]To this statement about extinguishment of junior liens in a nonjudicial foreclosure, we must attach a caveat. This holding is limited to this case and these facts. Because of our decision in this case, it is not necessary for us to discuss the constitutional implications inherent in Alabama's nonjudicial mortgage foreclosure statute which on its face permits extinguishment by a mortgagee of subordinate liens without any notice to those lienors except by publication in the newspaper. At this point in time, to the knowledge of this court, no court has held such a foreclosure statute unconstitutional. However, for a discussion of such a constitutional problem, see Federal Deposit Insurance Corporation v. Morrison, 747 F.2d 610 (11th Cir.1985),

this reason, it was impossible for Mid-State to conduct a second correcting foreclosure sale. It follows that when Southern Bank's and Mid-State's liens were extinguished, the tax liens, were naturally elevated from their junior status.

In our view, the appellees' failure to provide notice to the government of the sale and their subsequent purchase of the property has placed the government in a position to exercise any of its collection remedies including levy and seizure of the property. The appellees argue that this result is harsh and that it violates principles of equity.

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reh'g denied, 763 F.2d 419 (1985) (Clark J., dissenting with opinion); Note, Mortgages-Does Foreclosure Under Power of Sale Violate Due Process Rights?, 4 Cum.-Sam.L.Rev. 507 (1974); G. Osborne, G. Nelson and D. Whitman, Real Estate Finance Law Section 7.23 at 497 (1979).

Before we rule on their equitable arguments, we examine the legislative history of 26 U.S.C. Section 7425. It illustrates that the statute was designed to make a "provision for a timely notice to the Government where it has the status of a junior lienor and there is no plenary proceeding." Federal Tax Lien Act of 1966, S.Rep. No. 1708, 89th Cong., 2d Sess., reprinted in 1966 U.S.Code Cong. & Ad.News 3722, 2748. The Committee on Finance indicated that "[t]here [did] not appear to be any reason why in these cases there should not be a timely notice of the proceedings to the Government where notice of its tax lien is on file. The requirement of notice gives the Government an opportunity to review its position and determine the appropriate action without placing an undue burden on the foreclosing creditor." Id.

(emphasis added). In specifically discussing 26 U.S.C. Section 7425(b) it was observed:

> The bill provides that, in the case of all other foreclosure proceedings, where timely notice of the proceedings is given to the Government, the Government's claim to property under a tax lien is to be discharged in the manner provided by local law.
>
> Where foreclosures covered by this provision are made without proper notice to the Government, the bill provides that this does not affect the Government's claim under a tax lien (as where the Government is not joined in a judicial foreclosure). In these cases, the Government's claim continues against the property into the hands of a third party.

Id. at 3749.

One legal commentator, in seeking reform of the notice provisions, made the following observations:

> Notice of a sale enables the tax collector to drum up interest among potential bidders, to observe the fairness of the sale, and to reach the surplus proceeds, if any. Notice well in advance of the sale seems necessary only for the first of those purposes; but the tax collector is likely to utilize the

> opportunity to drum up bids only in the case of real property ... and in these cases 25 days may be too short to be meaningful.
>
> . . .
>
> [I]t seems desirable also to provide that the Government's remedy for inadequacy of the notice shall be only against the selling creditor, and that the innocent purchaser's title shall not be impaired if he behaved reasonably.

Plumb, Federal Liens and Priorities-Agenda for the Next Decade III, 77 Yale L.J. 1104, 1171-72 (1968) (emphasis added) (footnotes omitted).

Even if this commentator's suggestions for reform were adopted, Mid-State and Southern Bank would not prevail. The commentator advocates that the remedy for inadequate notice should be against the selling creditor rather than an innocent purchaser who behaved reasonably. E.g., as in Myers, supra. Mid-State and Southern Bank were neither innocent

purchasers nor did they behave reasonably under the circumstances.

Although appellees contend that our interpretation of the statute produces a harsh result, we think it is consistent with the plain language of the statute, the legislative history, and the overall purpose of our tax collection system. The appellees claim in each case the value of the property was much less than the amount of the debt, that I.R.S. in neither case would have paid off the debt if notice had been properly given, and that the government is unjustly enriched if it now has a first lien against the property. To accept appellees' argument would result in a disparate, unequal and impossible application of the federal notice statute. Appellees would have the notice statute apply only when the value of the land exceeded the mortgagor's debt

to the mortgagee. This would require litigation by the government of every non-notice case so that it would be able to conduct a comparison of the value of the security to the amount of the indebtedness. Congress required the simple expediency of notice by the mortgagee to the government prior to foreclosure in every case. We cannot and do not wish to rewrite the statute. Equitable principles do not persuade us to reach a contrary conclusion for the harsh results now imposed could have easily been avoided by Mid-State and Southern Bank.

Mid-State and Southern Bank, as mortgagees, were in the best position to provide notice to the government and extinguish the liens. If as in Myers, an innocent third party purchaser takes the property subject to the lien, these

experienced mortgagees certainly should not receive different treatment.

Our conclusion is bolstered by the supremacy clause of the United States Constitution which provides that:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

U.S. Const. Art. VI, cl. 2.

As the Supreme Court stated in Commonwealth Edison Company v. Montana, 453 U.S. 609, 634, 101 S.Ct. 2946, 2962, 69 L.Ed.2d 884 (1981) "[p]re-emption of state law by federal statute or regulation is not favored' in the absence of persuasive reasons-either that the nature of the regulated subject matter permits

no other conclusion, or that the Congress has unmistakably so ordained." Id.

The collection of taxes serves a vital national interest. The federal tax lien is one of the tools utilized by the government to achieve this ojective. Because of this important interest, we cannot permit states to nullify the effectiveness of the federal tax lien by enacting nonjudicial foreclosure laws or by applying various equitable principles recognized by the state. The legislative history of 26 U.S.C. Section 7425 makes clear that Congress did not intend such a result.

We therefore hold that the failure of the mortgagees to comply with the notice provisions of 26 U.S.C. Section 7425 before they conducted the foreclo-

sure sales and purchased the property, caused their mortgage liens to be extinguished and the federal liens to be elevated from their junior status.

C. Property Interest to which the Tax Lien Attached

[2] One issue we must decide is whether each taxpayer had a sufficient property interest for the federal tax liens to attach to the underlying property.

The appellees argue that Alabama classifies itself as a "title" state with regard to mortgages. Thus, "[e]xecution of a mortgage passes legal title to the mortgagee. The mortgagor is left with an equity of redemption, but upon payment of the debt, legal title revests in the mortgagor." Trauner v. Lowrey, 369 So.2d 531, 534 (Ala.1979) (citations omitted). The equity of redemption is extinguished by a valid foreclosure sale. Thus, a

"mortgagor or his vendee is left only with the statutory right of redemption." Id.

Because Alabama follows the title theory, the appellees contend that the only interest to which the liens could attach was each taxpayer's equity of redemption. When foreclosure occurred, each taxpayer was left with a statutory right of redemption. Thus, the appellees contend that the United States holds only a statutory right of redemption in the property.

According to the appellees, the United States, as a holder of a statutory right of redemption, could not claim legal title to the property prior to the foreclosure sale unless it paid the mortgage in full and cannot now seek to recover the property until it has paid the mortgage in full.

We agree with the appellees that under Alabama law the property interest held by each taxpayer was an equitable right of redemption. In Alabama, this is a valuable property interest for it may be conveyed by the mortgagor and it allows a mortgagor, who has retained possession of the subject property, to be possessed of legal title against all of the world except the mortgagee or its assignee. See Trauner v. Lowrey, 369 So.2d 531, 534 (Ala.1979); Jones v. Butler, 237 So.2d 460, 462 (Ala. 1970). We therefore conclude that each taxpayer had "property" and "rights to property" under 26 U.S.C. Section 6321 to which the tax lien could attach. See Little v. United States, 704 F.2d 1100, 1105 (9thCir.1983) for a discussion of a right of redemption being a "right to property" since such a right is an economic asset,

has a pecuniary worth, and is transferable.

In its brief, Mid-State relies upon Gilliland v. United States, 47 A.F.T.R.2d 1364, 81-1 USTC Para. 9322 at 86,83/ (M.D.Tenn.1981), arguing the following:

> In a dispute involving similar facts, the courts in Gilliland noted that since the taxpayer held only equitable rights to the property, the IRS' lien could attach solely to these rights. The court also noted that a foreclosure sale without notice to the IRS did not discharge the IRS' lien, which continued on after the sale.
>
> Appellee's Brief, No. 84-7501, at 8.

The court in that opinion held the following:

> However, it is clear that the lien did in fact attach to Webb's interests in the realty, even though those interests were equitable in nature. See Howard v. United States, 566 S.W.2d 521 (Tenn.1978) (federal tax lien attached to the equitable interest of income beneficiary in a spendthrift trust). And, since Webb's equitable interests in the property continued to exist until terminated by the foreclosure sale, the issue now before the court is whether that sale was

> also effective to extinguish the government's rights under the tax lien.
>
> * * * * *
>
> The foreclosure sale was precisely the kind of non-judicial sale contemplated by 26 U.S.C. Section 7425(b), and in the absence of the notice required by the statute, the sale could not operate to discharge the government's tax lien. The tax lien, having previously attached to Webb's equitable interests in the subject property, clearly survived the trustee's foreclosure sale.

Gilliland, Para. 9322 at 86,840.

The contention by the appellees that the government had only a statutory right of redemption inferior to their title is meritless. The interest of the government after the foreclosure sale was that of an enforceable lien against the realty in each instance and Alabama's statutory redemption provisions have no application to this case.

IV. CONCLUSION

The judgment of the district court in each case is reversed. In reversing, we do not divest the district court of any jurisdiction it needs with respect to the enforcement of the government's tax liens.

REVERSED AND REMANDED.

EXHIBIT "D"

UNITED STATES COURT OF APPEALS

ELEVENTH CIRCUIT
OFFICE OF THE CLERK
50 Spring Street, S.W.
ATLANTA, GEORGIA 30303

December 5, 1985

TO ALL PARTIES LISTED BELOW:

NO. 84-7280 - SO. BANK OF LAUDERDALE CTY. v. IRS, USA
(DC No. 82-HM-5236-NW)
84-7501 - MID-STATE HOMES, INC. v. USA
(DC No. CV83-AR-1072-S)

This is to advise that an order has this day been entered denying the petition( ) for rehearing.

No member of the panel nor judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure, Eleventh

Circuit Rule 26), the petiton( ) for rehearing en banc has also been denied.

See Rule 41, F.R.A.P., and Eleventh Circuit Rule 27 for issuance and stay of the mandate.

Sincerely,

SPENCER D. MERCER,
Clerk

By:/s/ Denza F. Bankhead
Deputy Clerk

cc w/enclosure to:

Mr. Frank W. Donaldson, U.S. Attorney, Birmingham, AL
Ms. Caryl P. Privett, AUSA, Birmingham, AL
Mr. Glenn L. Archer, Jr., Asst. Atty. Gen.
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Mr. John E. Higginbotham, Esq.
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Mr. James M. Edwards, Esq.

IN THE UNITED STATES COURT OF APPEALS

FOR THE ELEVENTH CIRCUIT

NOS. 84-7280, 84-7501

SOUTHERN BANK OF LAUDERDALE COUNTY,

Plaintiff-Appellee,

versus (filed Dec. 5, 1985)

INTERNAL REVENUE SERVICE, UNITED STATES OF AMERICA,

Defendants-Appellants.

MID-STATE HOMES, INC.,

Plaintiff-Appellee,

versus

UNITED STATES OF AMERICA,

Defendant-Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE MIDDLE DISTRICT OF ALABAMA

ON PETITION FOR REHEARING AND
SUGGESTION FOR REHEARING EN BANC

(Opinion September 13, 1985, 11 Cir., 1985, _____F.2d_____).

(December 5, 1985)

Before KRAVITCH and CLARK, Circuit Judges, and WRIGHT[1], Senior Circuit Judge.

PER CURIAM:

The Petition for Rehearing is DENIED and no member of this panel nor other Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure; Eleventh Circuit Rule 26), the Suggestion for Rehearing En Banc is DENIED.

ENTERED FOR THE COURT:

/s/ Thomas A. Clark
United States Circuit Judge

---

[1]Honorable Eugene A. Wright, U.S. Circuit Judge for the Ninth Circuit, sitting by designation.

EXHIBIT "E"

Section 7425. DISCHARGE OF LIENS.

(a) Judicial Proceedings.-If the United States is not joined as a party, a judgment in any civil action or suit described in subsection (a) of section 2410 of title 28 of the United States Code, or a judicial sale pursuat to such a judgment, with respect to property on which the United States has or claims a lien under the provisions of this title-

(1) shall be made subject to and without disturbing the lien of the United States, if notice of such lien has been filed in the place provided by law for such filing at the time such action or suit is commenced, or

(2) shall have the same effect with respect to the discharge or divestment of such lien of the United States as may be provided with respect to such matters by the local law of the place where such property is situated, if no notice of such lien has been filed in the place provided by law for such filing at the time such action or suit is commenced or if the law makes no provision for such filing.

If a judicial sale of property pursuant to a judgment in any civil action or suit to which the United States is not a party discharges a lien of the United States arising under the provisions of this title, the United States may claim, with the same priority as its lien had against the property sold, the proceeds (exclusive of costs) of such sale at any time before the distribution of such proceeds is ordered.

(b) Other Sales.-Notwithstanding subsection (a) a sale of property on which the United States has or claims a lien, or a title derived from enforcement of a lien, under the provisions of this title, made pursuant to an instrument creating a lien on such property, pursuant to a confession of judgment on the obligation secured by such an instrument,

or pursuant to a nonjudicial sale under a statutory lien on such property-

(1) shall, except as otherwise provided, be made subject to and without disturbing such lien or title, if notice of such lien was filed or such title recorded in the place provided by law for such filing or recording more than 30 days before such sale and the United States is not given notice of such sale in the manner prescribed in subsection (c)(1); or

(2) shall have the same effect with respect to the discharge or divestment of such lien or such title of the United States, as may be provided with respect to such matters by the local law of the place where such property is situated, if-

(A) notice of such lien or such title was not filed or recorded in the place provided by law for such filing more than 30 days before such sale,

(B) the law makes no provisions for such filing, or

(C) notice of such sale is given in the mannter prescribed in subsection (c)(1).

(c) Special Rules.-

(1) Notice of sale.-Notice of a sale to which subsection (b) applies shall be given (in accordance with

regulations prescribed by the Secretary) in writing, by registered or certified mail or by personal service, not less than 25 days prior to such sale, to the Secretary.

(2) Consent to sale.-Notwithstanding the notice requirement of subsection (b)(2)(C), a sale described in subsection (b) of property shall discharge or divest such property of the lien or title of the United States if the United States consents to the sale of such property free of such lien or title.

(3) Sale of perishable goods.-Notwithstanding the notice requirement of subsection (b)(2)(C), a sale described in subsection (b) of property liable to perish or become greatly reduced in price or value by keeping, or which cannot be kept without great expense, shall discharge or divest such property of the lien or title of the United States if notice of such sale is given (in accordance with regulations prescribed by the Secretary) in writing, by registered or certified mail or by personal service, to the Secretary before such sale. The proceeds (exclusive of costs) of such sale shall be held as a fund subject to the liens and claims of the United States, in the same manner and with the same priority as such liens and claims had with respect to the property sold, for not less than 30 days after the date of such sale.

(d) Redemption by United States.-

(1) Right to redeem.-In the case of a sale of real property to which subsection (b) applies to satisfy a lien prior to that of the United States, the Secretary may redeem such property within the period of 120 days from the date of such sale or the period allowable for redemption under local law, whichever is longer.

(2) Amount to be paid.-In any case in which the United States redeems real property pursuant to paragraph (1), the amount to be paid for such property shall be the amount prescribed by subsection (d) of section 2410 of title 28 of the United States Code.

(3) Certificate of redemption.-

(A) In General.-In any case in which real property is redeemed by the United States pursuant to this subsection, the Secretary shall apply to the office designated by local law, if any, for the documents necessary to evidence the fact of redemption and to record title to such property in the name of the United States. If no such officer is designated by local law or if such officer fails to issue such documents, the Secretary shall execute a certificate of redemption therefor.

(B) Filing.-The Secretary shall, without delay, cause such documents or certificate to be duly recorded in the proper registry of deeds. If the State in which the real property redeemed by United States is situated has not by law designated an office in which such certificate may be recorded, the Secretary shall file such certificate in the office of the clerk of the United States district court for the judicial district in which such property is situated.

(C) Effect.-A certificate of redemption executed by the Secretary shall constitute prima facie evidence of the regularity of such redemption and shall, when recorded, transfer to the United States all the rights, title, and interest in and to such property acquired by the person from whom the United States redeems such property by virtue of sale of such property.

CERTIFICATE OF SERVICE

I, Richard H. Gill, a member of the Bar of the Supreme Court of the United States and the attorney for Mid-State Homes, Inc., do hereby certify that on this the 3rd day of March, 1986, I did serve the requisite number of copies of the foregoing on the attorneys for all other parties in the Court of Appeals, by mailing the same to them first class, postage prepaid and addressed as follows:

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Supreme Court, U.S.
FILED
MAY 15 1986
JOSEPH F. SPANIOL, JR.
CLERK

No. 85-1546

In the Supreme Court of the United States

OCTOBER TERM, 1985

MID-STATE HOMES, INC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

CHARLES FRIED
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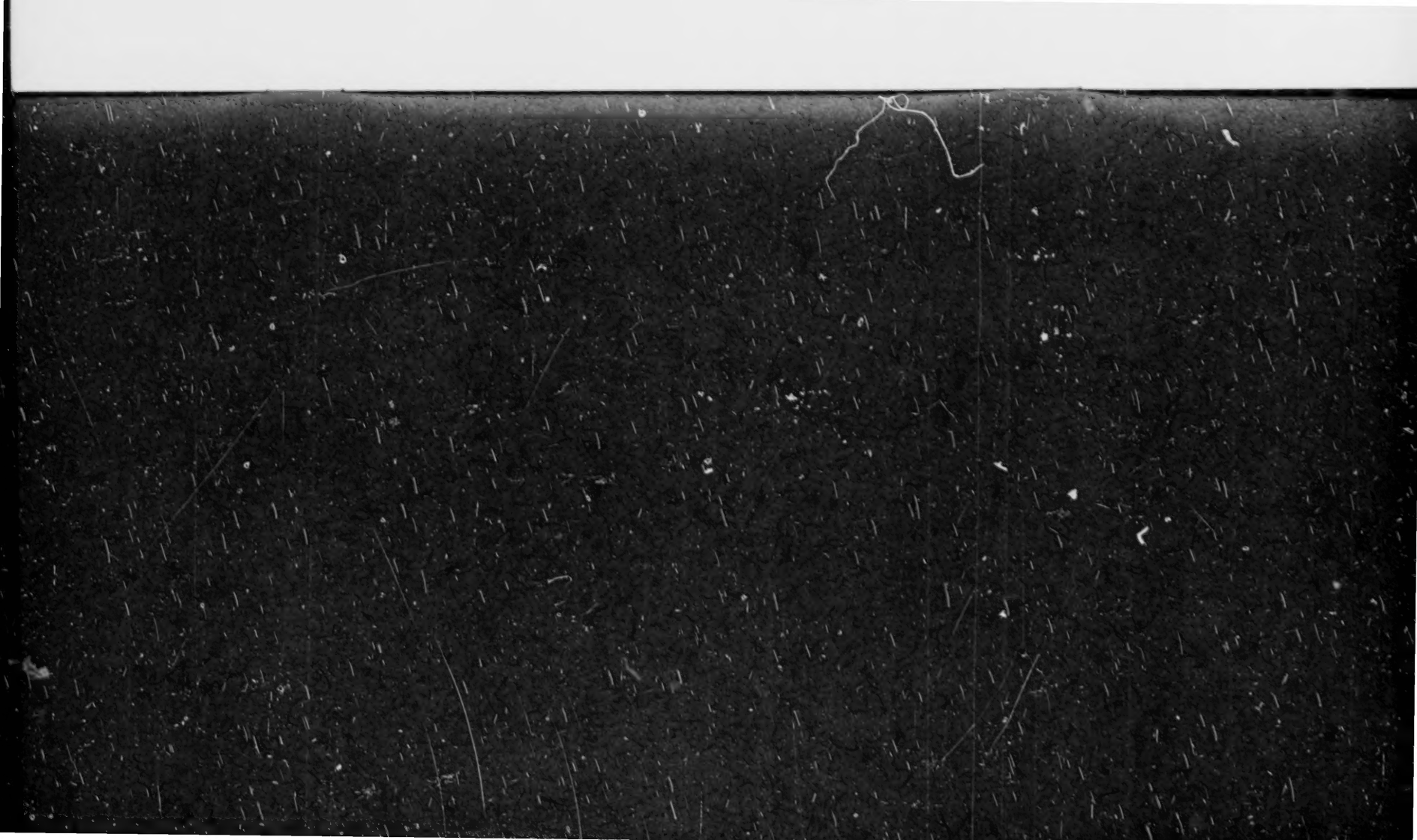

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In the Supreme Court of the United States

OCTOBER TERM, 1985

No. 85-1546

MID-STATE HOMES, INC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

Petitioner challenges the court of appeals' holding that its interest as a purchaser at a nonjudicial foreclosure sale held without notice to the United States is subject to a federal tax lien. The decision below is correct. Petitioner does not allege, nor is there, a conflict among the circuits on the question presented. There is no basis for further review.

1. In October 1972, taxpayers Manuel Ferguson and his wife executed a mortgage on Alabama realty (Pet. App. A6). The mortgage was later assigned to petitioner Mid-State Homes (*id.* at A7). In November 1979, the IRS made an asssessment of unpaid taxes against the Fergusons in the amount of $8,580 (*ibid.*). The IRS properly filed, on July 17, 1980, a notice of tax lien in that amount against the Fergusons' property (*ibid.*).

The Fergusons subsequently defaulted on their mortgage. On December 30, 1981, in accordance with the power of sale contained in the mortgage, petitioner conducted a nonjudicial foreclosure sale of the property (Pet. App. C6). Petitioner, however, failed to give the United States notice of the sale, as required by Section 7425(c)(1) of the Internal Revenue Code.[1] That Section provides that notice of a nonjudicial sale of property on which the IRS has a tax lien "shall be given * * * in writing * * * not less than 25 days prior to such sale, to the Secretary [of the Treasury]." Section 7425(b)(1) in turn provides that, if the IRS is not properly notified of a nonjudicial foreclosure sale, the sale "shall * * * be made subject to and without disturbing such lien." Petitioner purchased the Fergusons' property at the foreclosure sale for $12,543 (Pet. App. C7 & n.4).

Apparently recognizing that its foreclosure sale was ineffectual against the United States because of its failure to give the notice required by Section 7425, petitioner conducted another foreclosure sale of the same property about 11 months later (Pet. App. C7 & n.5). This time, petitioner gave notice of the sale to the United States. Petitioner once again purchased the property at the foreclosure sale (*id.* at A7-A8).

Section 6331(a) of the Code authorizes the IRS to collect an unpaid tax "by levy upon all property and rights to property * * * on which there is a lien * * * for the payment of such tax." On April 22, 1983, the IRS endeavored to collect the Fergusons' unpaid tax by levying on the property that petitioner had purchased at the foreclosure sale (Pet. App. A8). After the IRS took possession of the realty, petitioner brought this wrongful levy action in the district

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[1]Unless otherwise noted, all statutory references are to the Internal Revenue Code of 1954 (26 U.S.C.), as amended (the Code or I.R.C.).

court, seeking return of the property and contending inter alia that Section 7425 was unconstitutional (Pet. App. C12).

The district court entered summary judgment for petitioner (Pet. App. A1-A14). It held that "Mid-State's second foreclosure was successful in cutting off [the government's] tax lien, leaving [the government] with no more than a lien creditor's statutory right to redeem" (*id.* at A9). The court gave the government 30 days either to redeem the property or to relinquish possession (*id.* at A14).

The court of appeals unanimously reversed (Pet. App. C1-C42). It held that, since petitioner failed to notify the IRS of the first foreclosure sale, the plain language of the statute dictated that the sale was "made subject to and without disturbing" the federal tax lien (I.R.C. § 7425(b)(1)). Under Alabama law, the court continued (Pet. App. C25-C29), the result of petitioner's purchase of the property at the first foreclosure sale was to extinguish both the Fergusons' mortgage indebtedness and petitioner's mortgage lien, in effect "merging" the equity of redemption (previously held by the Fergusons) and the legal title (previously held by petitioner). By virtue of this "complete merger of title" (*id.* at C28), the first foreclosure sale vested petitioner with "fee simple title to the property," title that was "superior to all liens except those not extinguished, such as * * * [the] federal tax lien," which survived as a claim against the property on account of petitioner's noncompliance with Section 7425(b)(1). Since petitioner acquired a fee simple interest by virtue of the first foreclosure sale, the court concluded, "it was impossible for [petitioner] to conduct a second correcting foreclosure sale," and thus extinguish the federal tax lien, by purporting to sell to itself, some 11 months later, property that it already owned (Pet. App. C29).

The court of appeals acknowledged that the effect of its holding was to elevate the federal tax lien from its junior status and make it a senior claim against the property (Pet. App. C29). The court explained, however, that this was the natural and inevitable result of petitioner's failure to notify the IRS of the sale, as required by Section 7425, and the merger of title under Alabama law, under which the foreclosure sale extinguished petitioner's senior lien and converted that lien into a fee simple interest. The court rejected petitioner's argument that this result was "harsh and that it violate[d] principles of equity" (Pet. App. C29), pointing out that petitioner, as mortgagee, was "in the best position to provide notice to the government" and thereby to extinguish the tax lien (*id.* at C34). The court noted that, if an innocent third party had purchased the property at the first foreclosure sale, that third party would have taken the property "subject to" the federal tax lien by virtue of petitioner's noncompliance with Section 7425(b)(1). "[E]xperienced mortgagees" like petitioner, the court concluded, "certainly should not receive different treatment" when they purchase foreclosed-upon property themselves (Pet. App. C34-C35).

2. The court of appeals' decision is correct and is in accord with the decisions of every other court of appeals that has considered the question. Congress enacted Section 7425 in 1966 (Federal Tax Lien Act of 1966, Pub. L. No. 89-719, § 109, 80 Stat. 1141) in response to this Court's opinion in *United States* v. *Brosnan*, 363 U.S. 237 (1960). The Court there held that, if state law permitted it, a senior lienor could extinguish a junior federal tax lien by conducting a nonjudicial foreclosure sale without notifying the United States. Believing that the government's interests were not adequately protected in such circumstances, Congress enacted Section 7425 to govern the discharge of junior federal tax liens. Section 7425(b)(1) provides that, when

notice of a nonjudicial sale is not provided to the IRS, the sale shall "be made subject to and without disturbing [the federal tax] lien." The legislative history confirms that, in the absence of notice, the government may enforce its lien against the property in the hands of the person who purchases it at the foreclosure sale. See H.R. Rep. 1884, 89th Cong., 2d Sess. 72 (1966).

Now that the Eleventh Circuit has reversed the district court's judgment in this case, judicial authority is once again uniform as to the proper interpretation of Section 7425. That uniform view is that, if the United States is not given notice of a nonjudicial sale, the federal tax lien encumbers the property in the hands of the purchaser and, as between the purchaser and the United States, the United States comes first. *E.g., Myers* v. *United States*, 647 F.2d 591 (5th Cir. 1981); *Baldwin County S&L Ass'n* v. *United States*, 81-2 U.S. Tax Cas. (CCH) ¶ 9619 (S.D. Ala. 1981); *Puls* v. *United States*, 387 F. Supp. 760 (N.D. Cal. 1974); *Gilliland* v. *United States*, 47 A.F.T.R.2d (P-H) ¶ 81-589 (M.D. Tenn. 1981). See *Little* v. *United States*, 709 F.2d 517 (9th Cir. 1983); *Baum* v. *United States*, 76-1 U.S. Tax Cas. (CCH) ¶ 9208 (2d Cir. 1975). And this is so regardless of whether the purchaser at the foreclosure sale is an innocent third party (as in *Myers* v. *United States, supra*) or a former mortgagee of the property (as in the instant case and *Baldwin County S&L Ass'n* v. *United States, supra*). While arguing that the court of appeals' interpretation of Section 7425 is wrong (Pet. 12, 23-24), petitioner fails to address the uniform line of judicial authority in support of the decision below. Indeed, petitioner makes no claim that there is a conflict among the circuits on the question presented.

3. In challenging the correctness of the decision below, petitioner appears to have abandoned the argument on which the district court relied in granting it summary judgment—*i.e.*, that the "second foreclosure was successful

in cutting off [the government's] tax lien" (Pet. App. A9). Petitioner, in other words, seems to accept the court of appeals' conclusion that it would be "impossible for [petitioner] to conduct a second correcting foreclosure sale" (*id.* at C29) by purporting to buy property that it already owned. Petitioner challenges the decision below, rather, on the broader ground that the effect of its failure to notify the IRS of the first foreclosure was to render that sale "ineffectual and invalid" (Pet. 25), thereby returning petitioner and the IRS to their status quo ante the sale. Since the IRS's tax lien before the sale attached only to the Fergusons' equity of redemption, petitioner argues, the effect of its failure to notify the IRS under Section 7425 was not to subject petitioner's fee interest in the property to the government's tax lien, but was merely to cause "the [g]overnment's *equity of redemption* [to] continue[] after foreclosure" (Pet. 24-26 (emphasis in original)).

Petitioner's argument is squarely at odds with the plain language of the statute, with the uniform line of judicial decisions discussed above, and with the pertinent provisions of Alabama law as interpreted by the court of appeals. Section 7425 does not say that failure to notify the IRS nullifies a nonjudicial sale; the statute says, rather, that the nonjudicial sale in such circumstances "shall * * * be made subject to and without disturbing [the tax] lien" (I.R.C. § 7425(b)(1)). As we have noted, the courts of appeals have uniformly construed this statutory language to mean that the effect of a mortgagee's failure to notify the IRS is that the tax lien survives and encumbers the property in the hands of the purchaser—precisely the conclusion reached by the court of appeals here. And petitioner's argument that the effect of noncompliance with Section 7425 is merely to have "the [g]overnment's equity of redemption continue[] after foreclosure" (Pet. 25) ignores the pertinent provisions of state law. As the court of appeals held (Pet. App. C26-C29), a foreclosure sale under Alabama law results in a

complete merger of title; there accordingly exists no "equity of redemption" that could "continue after foreclosure." To the contrary, a foreclosure sale under Alabama law "vest[s] the fee simple title to the property in the mortgagee[]," and it is to that fee simple interest that the surviving federal tax lien must necessarily attach. Petitioner acknowledges, as it must,[2] that merger of title is "a generalized concept in Alabama" (Pet. 16), but argues somewhat confusingly that the court of appeals nevertheless "misinterpret[ed] the weight of the law with respect to the doctrine of merger as applied to cases similar to the present [case]" and so "misapplied Alabama law" (Pet. 17). That contention would not merit this Court's review even if it were correct, which it is not.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

CHARLES FRIED
Solicitor General

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[2]See, *e.g.*, *Baldwin County S&L Ass'n* v. *United States*, 81-2 U.S. Tax Cas. (CCH) at 88,065; *Muscle Shoals Nat'l Bank* v. *Hallmark*, 399 So.2d 297 (Ala. 1981); *Trauner* v. *Lowrey*, 369 So.2d 531, 534 (Ala. 1979); *Mobley* v. *Brundidge Banking Co.*, 347 So.2d 1347, 1352 (Ala. 1977); *Oden* v. *King*, 216 Ala. 504, 508-509, 113 So. 609, 612 (1927).